



Modes of governance and corporate taxation in the European Union

Claudio M. Radaelli and Ulrike S. Kraemer
UNIVERSITY OF EXETER

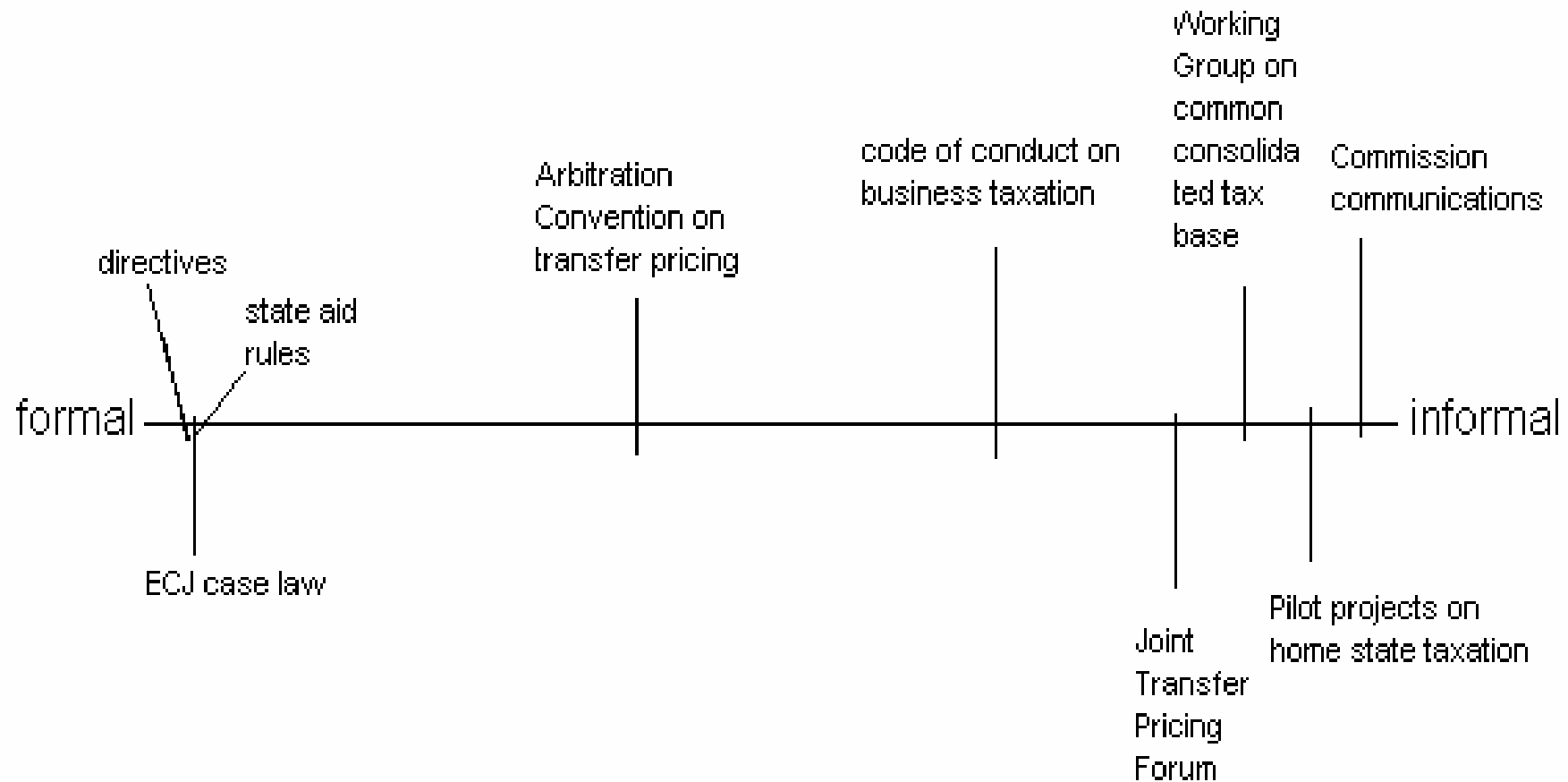
Essex Tax Workshop
6-7 July 2005



The problem

- Intensification of EU activity in direct corporate taxation since 1996 (box 1)
- Specific activities draw on different modes of governance, such as hard law (Community method), informal governance in the shadow of hierarchy, soft law, learning forums. Plus we have to account for ECJ's impact on tax governance (fig. 1)
- How do we explain the selection of modes of governance?
- Loads of academic rhetoric on new modes of governance and participation, learning, deliberative democracy, etc

FIG 1: A continuum from formal to informal governance modes





How do we explain the selections of different modes?

- Time as criterion to sort modes out?
- But what about the logic?
- And how does one classify modes?
- Additionally, new modes are nested amongst more traditional modes

Code of conduct, directive on royalties, savings directive

Tax package (1997-2003)



Three alternative hypotheses

H1 = Constellations of EU actors choose modes of governance in order to increase the **problem-solving capacity** of tax policy

H2 = Constellations of EU actors choose modes of governance in order to increase **social legitimacy**

H3 = Constellations of EU actors choose modes of governance in order to reduce **political transaction costs**



Entering political logic

- In highly contested issue areas, new modes are chosen in order to avoid political transaction costs
- We confirm this hypothesis for the EU - new governance as political expedient. Although it has some structural similarities with the OMC the logic is not learning
- But can we say something more about this political logic?



New governance or new politics?

- From a focus on new – old governance
- To a focus on changing political strategies
- Our question is 'new governance or new politics' (that is, political logics and how they change)?
- 'Changing political logic' is our independent variable. Modes of governance are the dependent variable



The emergence of modes of governance

- Legacy of the past and learning points for the Commission:
 - problems of governance systems that are unbalanced in terms of power relations ('tax neutrality', 'harmful tax competition' are unbalanced)
 - Commission has the problem that when it gets one actor on board, it loses the other actor
 - Difficult but indispensable to avoid capture



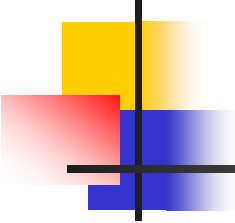
Our model

- Focus on actors in the EU institutional settings. Institutions reduce empirical variance (actor-centred institutionalism)
- Material pressure: 'globalisation'; ECJ
- Ideational pressure: discourses about harmful tax competition, tax neutrality, corporate tax reform as antagonistic political projects pushed by specific constellations of actors



The role of the Commission

- Commission has process goals but also an aim in terms of outcome, i.e., to balance power relations and avoid capture by either the MS or the business Community
- It is impossible to balance tax governance at the systemic level: unanimity, plus there are no institutional fora for discussing the concept of tax governance, see 2005 failed Lux initiative for a dedicated Council formation
- So what we see is the emergence of functionally differentiated governance arenas at the sub-systemic level



Functionally differentiated governance arenas

- They follow different political logics
- They select their own policy problems
- They chose their own policy instruments
- They define their own mix of modes of governance

They differ in important dimensions:

- Participation
- Problem-solving efficiency
- Accountability
- Transparency



Governance arenas

1. Harmful tax competition
2. Corporate tax reform
3. Emerging arena: Politics of ECJ tax jurisprudence



Harmful tax competition

Actors: Member States, Commission

Material Pressure: Globalisation, deep economic integration in the single market

Ideational variables: narrative of harmful tax competition

Selection of modes of governance: politically contingent (see tax package)



Assessment

Code of conduct, state aids, and savings directive have established some principles and contributed to a change in the overall climate for international business and domestic tax policy

Domestic policy changes under way at Man, Jersey, Estonia expose the limits of what can be achieved

Savings directive

“Scores” in terms of participation and perceptions of legitimacy are low

Lack of political interest at the moment, some participants see this arena as ‘the past’



Corporate tax reform

Actors: Commission, Commissioners (change from Monti to Bolkestein), business community, MS

Material Pressure: deep economic integration in the single market sheds light on tax obstacles and inconsistencies (transfer pricing, etc)

Ideational variables: single market, EU competitiveness, red tape and administrative burdens

Selection of modes of governance: preference for participatory modes, although MS always reluctant (see case of base coordination)



Assessment

- Several projects, like Home State Taxation, Base Harmonisation, Transfer Prices Forum
- Technical difficulties compounded by diverging political views (France, Germany versus UK, Estonia)
- Participants expect slow progress (more than 5 years at least)



The paradox of tax governance

- Harmful tax competition arena will not make additional progress
- Corporate tax reform arena is projected onto the future
- Political interest in EU tax coordination is dwindling. Impossible to coordinate tax policy at the macro systemic level due to unanimity and the opposition to a possible EU tax governance body



But there is no political vacuum in politics... entering the third emerging arena

- ECJ jurisprudence as major pressure on MS
- Commission's attempts to make political capital out of the ECJ have found a lukewarm response from the MS
- Indeed, new cases are problematic for the Commission (IRAP), if anything there may be a loss of political capital
- UK statement that they will rein in the ECJ during their Presidency is not realistic, they tried already with the Constitution (tax carve-out)
- So MS are punished politically by the ECJ. MS could respond to this by strong coordination at the EU level, but this is precisely why they do not want to do



Implications for TJN

- No presence in the ideational context. HTC has potential for the articulation of the public interest in EU taxation, but this is not the emerging arena and in any case it is the most secretive and less open
- No participation in new forums such as the transfer pricing forum, designed to address the problems of multinationals, not the political issues of t.p.
- New Commissioner may be interested, but he is seen as a minor player with a small portfolio
- Possible use of state aids procedure
- Consider instigating ECJ cases on tax transparency, boardroom tax policies, etc. But where is the legal base for this action?